

From: *Abhay Padgaonkar*
 Date: February 8, 2021
 Docket: APS Rate Review (E-01345A-19-0003); APS Rate Case (E-01345A-19-0236)
 Re: **The Commission Must Account for APS's Non-MEP \$100+ Million Annual Windfall**

Dear Commissioners:

You may recall that APS has steadfastly minimized the impact customers not on their Most Economical Plan (MEP) have on its "overearning," which APS has claimed does not exist. Last year, Pinnacle West's CFO Ted Geisler even went as far as telling the investors that the difference in the bills on or off the MEP is "de minimis" (so minor as to merit disregard) and that "it's difficult to read too much into the proportion of customers that are or are not" on their MEP.¹

Both these APS's assertions, however, are severely contradicted by the MEP data APS has released in its Fourth Quarter 2020 Quarterly Customer Outreach Report.² The reality is this: APS has been cashing in on \$100+ million annual windfall from transitioning, steering, and keeping the non-MEP customers on more expensive plans. One constant that has remained unchanged is that nearly half of APS's residential customers are still not on their MEP. This enormous windfall on the backs of captive ratepayers constitutes a significant percentage of APS's Net Income.

This Commission must account for this massive surplus, regardless of whether it is technically considered "overearning," by reducing the Revenue Requirement and/or the ROE in the pending APS rate case.

APS is generating a \$100+ million annual windfall

APS has repeatedly dodged answering this simple question: How much surplus revenue is APS generating from the non-MEP customers? Last year, Commissioner Kennedy computed the surplus revenue as \$171.3 million annually based on about half or 571,000 customers paying an average of \$25 more per month for 12 months.³ The following table, derived from the MEP data in APS's report, answers the question: The analysis shows that APS is overearning **\$103.7 million in surplus revenue annually** from non-MEP customers.

APS ANNUAL REVENUE OVEREARNING FROM NON-MEP CUSTOMERS								
Rate Plan	# of Cust	\$0-\$5	\$5-\$10	\$10-\$15	\$15-\$20	\$20-\$25	>\$25*	Total
R-XS	305,940	\$ 458,910	\$ 550,692	\$ 458,910	\$ -	\$ -	\$ -	\$ 1,468,512
R-Basic	93,234	\$ 615,344	\$ 839,106	\$ 839,106	\$ 783,166	\$ 503,464	\$ 1,846,033	\$ 5,426,219
R-Basic-L	22,137	\$ 6,641	\$ 59,770	\$ 232,439	\$ 557,852	\$ 657,469	\$ 9,642,877	\$ 11,157,048
R-TOU-E	355,623	\$ 1,813,677	\$ 7,041,335	\$ 8,534,952	\$ 6,721,275	\$ 5,761,093	\$ 42,248,012	\$ 72,120,344
R-2	92,946	\$ 892,282	\$ 1,505,725	\$ 1,394,190	\$ 975,933	\$ 501,908	\$ 1,226,887	\$ 6,496,925
R-3	227,482	\$ 614,201	\$ 818,935	\$ 1,023,669	\$ 955,424	\$ 614,201	\$ 3,002,762	\$ 7,029,194
TOTAL	1,097,362	\$ 4,401,056	\$ 10,815,564	\$ 12,483,266	\$ 9,993,650	\$ 8,038,135	\$ 57,966,572	\$103,698,242

* APS has, again, failed to define what it arbitrarily calls '>\$25'. It is assumed to be \$55 per month in this analysis as '>\$25' typically implies large users of electricity.

¹ "Pinnacle West Q1 2020 Results - Earnings Call Transcript" at: <https://www.fool.com/earnings/call-transcripts/2020/05/09/pinnacle-west-capital-corp-pnw-q1-2020-earnings-ca.aspx>

² APS 2020 Quarter 4 Customer Outreach Report on 2/1/2020 at: <https://docket.images.azcc.gov/E000011583.pdf>

³ ACC Open Meeting on 8/5/2020 starting at the 3:25:00 mark with Comm. Kennedy asking questions: https://azcc.granicus.com/player/clip/4054?view_id=3&redirect=true&entrytime=12300

APS is entirely responsible for generating this \$100+ million annual windfall

While APS is quick to blame the customers' lifestyle or unwillingness to change, the fact remains that APS has carefully engineered the current situation. The following deliberate actions and inactions by APS expose the serious weakness in APS's argument that — not APS — but its customers are to blame.

- **Flawed Rate Design:** 100% of customers on R-BASIC-L, 88% of customers or 313,000 customers on R-TOU-E (ironically named "Saver Choice"), nearly 70% of customers on R-2, and 47% of customers on R-BASIC are STILL not on their MEP nearly 3.5 years after the 2017 rate increase. In all, more than half a million customers are still not on their MEP. APS's devious rate design forced customers with >1,000 kWh/month usage onto a mandatory time-of-use rate plan, thereby blocking them from being on a simple, flat-rate plan. The flawed rate design has essentially trapped hundreds of thousands of customers on the highly uneconomical R-TOU-E plan. The only other choice they have? Go on a scary demand-based plan that they don't understand and cannot manage.
- **Deceptive Rate Transitioning:** With its deviously flawed rate design, APS had already made the "most like" rate plans (like R-TOU-E) for a large majority of customers to be more expensive. Under the guise of transitioning them to the "most like" plan after the 2017 rate increase, APS knowingly defaulted 56% or nearly 375,000 — or 1 out of 3 — customers to a more expensive plan. Most of these trapped customers never figured out what hit them.
- **Faulty Rate Comparison Tool:** In 2019, APS admitted that its rate comparison tool was providing "overstated projections" at the time of the rate increase in August 2017.⁴ As Comm. Kennedy has noted, "the evidence shows the tool has been faulty from the very start"⁵ even before I exposed in November 2019 the fact that the malfunctioning tool was steering customers to more expensive plans. The flawed rate comparison tool has actively misled and overtly steered hundreds of thousands of captive ratepayers onto far more expensive rate plans.
- **Delayed Pro Forma Billing:** APS took zero initiative after the 2017 rate increase to provide pro forma billing to educate the customers about how much they would save, given their actual usage during each month, if the customers were on their most economical plan. APS complied only after being ordered to do so by the Commission in June 2019 via Decision No. 77270.⁶ And even then, APS took its sweet time (8 months) to implement only in March 2020. APS's frenzied, do-gooder activity since then—with the rate case pending—ought not to fool anyone.
- **Botched Customer Education and Outreach Plan:** In fact, according to the Barbara Alexander Report,⁷ APS's Customer Education Plan was a dismal failure because it "failed to include essential components of a reasonable customer education plan or program given the monumental task that the Company stated it could achieve." The evaluation further concluded that the APS Plan "failed to identify risks and barriers to achieve its intended goals and objectives" and that "APS's Education Plan failed to establish any measurable performance metrics or results to enable a determination of the effectiveness of the Plan."

Bottom Line: Most, if not all, of these broken elements will be carried into the pending APS rate case, and the massive windfall will continue indefinitely. If this surplus revenue did not have ACC jurisdictional costs associated with them, it would have fallen straight to APS's bottom line. Surplus earnings of \$104 million would have accounted for nearly 18% of APS's \$589 million Net Income in 2018. It may even partly explain why APS's revenue increased by \$131 million in 2018 *despite* only a \$95 million rate increase and a \$120 million tax expense refund. This Commission must account for this massive surplus, regardless of whether it is technically "overearning," by reducing the Revenue Requirement and/or the ROE in the pending APS rate case.

⁴ APS Response at: <https://docket.images.azcc.gov/E000004180.pdf>, 1

⁵ Comm. Kennedy's Letter dated December 13, 2019" at: <https://docket.images.azcc.gov/E000004091.pdf>, 1-2

⁶ ACC Decision No. 77270 at: <https://docket.images.azcc.gov/0000198805.pdf>

⁷ Evaluation of the APS Customer Education Plan by Barbara Alexander at: <https://docket.images.azcc.gov/E000006584.pdf>